

THOMAS E. MOSS
United States Attorney

JAMES C. STRONG
james.c.strong@usdoj.gov
ISB # 7428
U.S. Department of Justice, Tax Division
Post Office Box 7238, Ben Franklin Station
Washington, DC 20044
Telephone: (202) 514-9953
Facsimile: (202) 514-6770

Attorneys for the Plaintiff, United States

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF IDAHO

UNITED STATES OF AMERICA,)	
)	
Plaintiff,)	
)	
v.)	Civil No. 4:09-cv-00547
)	
PENNY LEA JONES, a/k/a PENNY)	
LEA WARDROP,)	
)	
Defendant.)	

COMPLAINT FOR PERMANENT INJUNCTION AND OTHER EQUITABLE RELIEF

Plaintiff, the United States for its complaint against Penny Lea Jones, also known as Penny Lea Wardrop, alleges as follows:

1. This is a civil action brought by the United States under 26 U.S.C. §§ 7402(a), 7407, and 7408 to enjoin Penny Lea Jones and anyone in active concert or participation with her, from the following activities:

- a. Preparing or filing, or assisting in, or directing the preparation or filing of any federal tax return, amended return or other related documents or forms for any other person or entity;
- b. Directly or indirectly organizing, promoting, marketing or selling any plan or arrangement that advises or assists taxpayers to attempt to violate the internal revenue laws or unlawfully evade the assessment or collection of their federal tax liabilities, including promoting, selling or advocating the use of false Forms 1099 or other false IRS forms based on the false claim that:
 - i. Taxpayers can draw on the Treasury of the United States to pay their tax debt or other debts using Forms 1099-OID or other documents;
 - ii. Taxpayers can issue false Forms 1099 to a creditor and report the amount on the false Form 1099 as income taxes withheld on their behalf;
 - iii. Taxpayers have a secret account with the Treasury Department, which they can use to pay their debts or which they can draw on for tax refunds through a process that is often termed “redemption” or “commercial redemption” by promoters of this tax-fraud scheme.
- c. Engaging in conduct subject to penalty under 26 U.S.C. § 6700, including organizing or selling a plan or arrangement and making or furnishing a

statement regarding the excludability of income or securing any other tax benefit that she knows or has reason to know is false or fraudulent as to any material matter;

- d. Engaging in conduct subject to penalty under 26 U.S.C. § 6701, including preparing and filing tax returns and other documents that understate the tax liabilities of others;
- e. Preparing her own federal income tax returns claiming income withholding and refunds based on amounts shown in Forms 1099 issued to her creditors;
- f. Filing, providing forms for, or otherwise aiding and abetting the filing of frivolous Forms 1040, Forms 1040X or Forms 1099 or other IRS forms for herself or others;
- g. Giving tax advice or assistance to anyone, and representing anyone other than herself before the Internal Revenue Service, and;
- h. Engaging in any other conduct that is subject to penalty under the Internal Revenue Code or that interferes with the proper administration and enforcement of the internal revenue laws.

Jurisdiction and Venue

- 2. Pursuant to 26 U.S.C. §§ 7402, 7407, and 7408, this action has been requested by the Chief Counsel of the Internal Revenue Service, a delegate of the Secretary of the Treasury, and is brought at the direction of the Attorney General of the United States.

3. Jurisdiction is conferred on this Court by 28 U.S.C. §§ 1340 and 1345 and 26 U.S.C. §§ 7402(a), 7407, and 7408.
4. Venue is proper in this Court pursuant to 28 U.S.C. § 1391 because Defendant Penny Lea Jones resides and does business in Idaho Falls, Idaho within this judicial district. Penny Lea Jones was previously known as Penny Lea Wardrop.

Defendant's Activities

5. Beginning in 2009, Penny Lea Jones has run a fraudulent tax return preparation business, using a post office box in Shelley, Idaho. Before relocating to Idaho, Jones formerly did business as Penny Wardrop Accounting and Tax Services, in Buellton, California.
6. In 2009, Penny Lea Jones prepared and filed frivolous tax returns, amended tax returns, and other frivolous documents on behalf of others in exchange for compensation. Jones signed her customers' frivolous tax returns as the paid return preparer.

Jones's Tax-Fraud Scheme

7. Jones promotes a tax-fraud scheme that involves filing frivolous tax returns and other frivolous documents with the IRS on behalf of her customers.
8. The returns Jones prepares for her customers fabricate the amount of federal income tax withheld on behalf of her customers. The fabricated tax withholding reported to the IRS on her customers' returns results in fraudulent refund claims by her customers.
9. In support of the fraudulent refund claims, Jones will file bogus Forms 1099-OID with the IRS.
10. Original issue discount (OID) income refers to the difference between the price for which a debt instrument is issued and its stated redemption price at maturity. OID income is

generally included in a taxpayer's income as it accrues over the term of a debt instrument, regardless if the taxpayer receives payments from the issuer of the debt instrument. OID income is treated like a payment of interest and a party issuing a financial instrument generating OID income must issue a Form 1099-OID.

11. The federal income tax returns that Jones prepares falsely state that her customer either issued a debt instrument that generated OID income or purchased a debt instrument that generated OID income.
12. The federal income tax returns that Jones prepares also falsely state that federal income taxes were withheld for the full amount of OID income purportedly received by her customer.
13. The frivolous federal income tax returns that Jones prepares list OID income purportedly received by her customer to or from a creditor of the customer, usually a car loan, mortgage or credit card balance owed by the customer to the creditor. The federal income tax returns Jones prepares also report tax withholding for near the amount of the debt. The result of this is an inflated tax liability for the customer but with a huge false refund claim.
14. Consequently, Jones's customers fail to file proper federal income tax returns and falsely claim tax refunds to which they are not entitled.
15. The apparent purpose of Jones's frivolous tax returns and Forms 1099-OID is to request fraudulent refunds by accessing a non-existing Treasury account.
16. In reality, Jones's scheme fraudulently reports that tax was withheld on behalf of her customers and then claims refunds based on that non-existent withholding.

17. The returns that Jones submits on behalf of her customers falsely claim that her customer withheld near the total amount of fraudulent Forms 1099-OID attached to the tax return (for each Form 1099-OID, Jones usually deducts a uniform amount from the amount reported as OID as the amount of tax withheld). The amounts listed on the Forms 1099-OID are based on the total amount of debt the customer owes to his/her creditor.
18. For example, in 2009, Jones prepared a 2005 amended tax return and 2008 tax return for Reginald and Julia Pasteur of Newport, North Carolina. On their 2005 amended tax return, Jones falsely claimed that the Pasteurs earned OID income of \$85,366. Likewise, for 2008, Jones reported that the Pasteurs earned \$347,874 as OID income. Jones submitted nine phony Forms 1099-OID with the returns, including Forms 1099-OID that claimed that the Pasteurs received original-issue discount income issued by North Carolina Centralized Collections as a result of a debt instrument for “child support payments.” The other Forms 1099-OID in 2005 and 2008 are for loans, mortgages and bank accounts of the Pasteurs. As a result of these false claims, the Pasteurs claimed fraudulent refunds of \$68,399 (2005) and \$250,246 to which they were not entitled.
19. Again in 2009, Jones prepared a 2005 income tax return for Troy Madoo of Brookeville, Maryland. On his tax return, Jones falsely claimed that Madoo earned OID income of \$561,199. Jones also submitted nine phony Forms 1099-OID claiming that Madoo had received \$561,199 of OID income and that \$560,299 of federal income tax had been withheld (on each Form 1099-OID, Jones had subtracted \$100 from the amount of OID income as the amount of income tax withheld). The phony Forms 1099-OID were purportedly issued to cover several credit cards, a car loan, a line of credit and a bank

account. As a result of these false claims, Madoo claimed a fraudulent refund of \$327,580 to which he was not entitled.

20. Also in 2009, Jones prepared an amended 2006 federal income tax return for James and Marilou Olsen of Oxnard, California. The stated reason for the amended return was that “changes due to Forms 1099-OID not previously filed.” On the Olsens’ amended return, Jones falsely claimed that they earned OID income in 2006 of \$1,274,916. Jones also submitted nine phony Forms 1099-OID falsely claiming that the Olsens had received \$1,274,916 of OID income and that \$1,274,016 of federal income tax had been withheld on their behalf. The phony Forms 1099-OID provide that they are issued because of loans and bank accounts. As a result of these false claims, the Olsens claimed a fraudulent refund for \$842,504 to which they were not entitled.
21. Jones does not limit her preparation of false federal income tax returns and phony Forms 1099-OID to her customers. In 2009, Jones prepared an amended 2007 federal income tax return on behalf of herself and her husband, Kevin Jones. Jones falsely claimed that they earned OID income in 2007 of \$363,568 and then submitted three phony Forms 1099-OID falsely claiming that they had \$363,557 of OID income and that \$363,407 of federal income tax had been withheld on their behalf (on each Form 1099-OID, Jones had subtracted \$50 from the amount of OID income as the amount of income tax withheld). As a result of these false claims, the Joneses claimed a fraudulent refund for \$74,546 to which they were not entitled.

Harm Caused by Jones's Misconduct

22. The IRS has identified at least 319 individual returns and 14 business returns prepared and/or filed by Jones in 2009 that request refunds based on Jones's fraudulent returns prepared and filed by Jones's business on behalf of customers located throughout the United States, including California, Ohio, Maryland, and Florida. The fraudulent refunds sought through these returns exceeds \$93 million.
23. Jones's scheme is part of a growing trend amongst tax defiers to file frivolous tax returns and Forms 1099-OID with the IRS and courts in an attempt to escape their federal tax obligations and steal from the U.S. Treasury.
24. The apparent purpose of Jones's frivolous IRS Forms 1040 and IRS Forms 1099-OID is to purport to satisfy the tax return filing requirements of the customer and lay the foundation for large refund requests or for the purpose of purporting to satisfy the taxpayer's tax obligations or other personal debts.
25. The returns that Jones submits on behalf of her customers falsely claim that her customer withheld an amount listed on fraudulent Form 1099-OID that Jones prepares and attaches to the tax return. The amounts listed on the Forms 1099-OID are based on the total amount of debt the customer owes to his/her creditors.
26. While the IRS is able to detect and stop most fraudulent refund claims, Jones's fraudulent tax return preparation has resulted in the IRS's issuance of at least \$4.3 million in erroneous refunds to her customers.
27. In addition to the lost revenue due to the issuance of erroneous refunds, the government has also incurred the expense of conducting the investigation of Jones's fraudulent return

preparation and responding to and processing the frivolous documents Jones submitted to the IRS.

28. In reliance on Jones's services, her customers have failed to file proper federal income tax returns, which has either deprived her customers of proper tax refunds to which they may have been entitled or deprived the United States of additional tax revenue owed by her customers.
29. Furthermore, Jones failed to provide the IRS with copies of returns or claims or a list of all returns and claims, that Jones prepared since December 31, 2005 as the IRS requested on August 20, 2009 under 26 U.S.C. § 6107(b).

Count I: Injunction Under 26 U.S.C. § 7407

30. The United States incorporates by reference the allegations contained in paragraphs 1 through 29.
31. The United States may seek an injunction against any tax return preparer who has engaged in any "fraudulent or deceptive conduct which substantially interferes with the proper administration of the Internal Revenue laws," or who has "engaged in any conduct subject to penalty under section 6694 or 6695." 26 U.S.C. § 7407.
32. If a return preparer's misconduct is continual or repeated and the court finds that a narrower injunction (i.e. prohibiting specific enumerated conduct) would not be sufficient to prevent the preparer's interference with the proper administration of federal tax laws, the court may enjoin the person from further acting as a return preparer.
33. Jones has repeatedly prepared and filed with the IRS false and fraudulent income tax returns on behalf of her customers.

34. As a result, Jones has repeatedly engaged in fraudulent or deceptive conduct which substantially interferes with the proper administration of the Internal Revenue laws.
35. Jones has repeatedly and continually prepared and filed federal tax returns that understate her customers' tax liabilities as a result of unreasonable and frivolous claims and has thus engaged in conduct subject to penalty under 26 U.S.C. § 6694.
36. Jones has repeatedly and continually prepared and filed federal tax returns that understate her customers' tax liabilities either as a willful attempt to understate her customers' tax liabilities or because of Jones's reckless and/or intentional disregard of the internal revenue laws and regulations.
37. Jones has continually engaged in conduct subject to penalty under 26 U.S.C. § 6695 by not complying with the IRS's request pursuant to 26 U.S.C. § 6107(b) that Jones provide to the IRS a customer list or copies of all federal tax returns prepared by her since December 31, 2005.
38. Injunctive relief is appropriate to prevent this misconduct because, absent an injunction, Jones is likely to continue to prepare false federal income tax returns and engage in other misconduct of the type described in this complaint.
39. Jones should be permanently enjoined under 26 U.S.C. § 7407 from acting as a federal tax return preparer because a more limited injunction would be insufficient to stop her from interfering with the proper administration of the tax laws.

Count II: Injunction Under 26 U.S.C. § 7408 for Violations of 26 U.S.C. §§ 6700 and 6701

40. The United States incorporates by reference the allegations contained in paragraphs 1 through 39.

- 41 The United States may seek an injunction to enjoin any person from, *inter alia*, entering in conduct subject to penalty under 26 U.S.C. §§ 6700 or 6701 if injunctive relief is appropriate to prevent recurrence of that conduct.
42. Section 6700 of the Internal Revenue Code imposes a penalty on any person who organizes or participates in the sale of a plan or arrangement and in so doing makes a statement with respect to the allowability of any deduction or credit, the excludability of any income, or the securing of any tax benefit by participating in the plan or arrangement which that person knows or has reason to know is false or fraudulent as to any material matter.
43. In 2009, Jones organized and participated in the sale of a plan or arrangement and in doing so made false and fraudulent statements with respect to the tax benefits of participating in the plan or arrangement which Jones knew or had reason to know were false.
44. As a result, Jones engaged in conduct subject to penalty under 26 U.S.C. § 6700.
45. Section 6701 of the Internal Revenue Code imposes a penalty on any person who aids or assists in, procures, or advises with respect to, the preparation of any portion of a return, affidavit, claim, or other document, who knows (or has reason to believe) that such portion will be used in connection with any material matter arising under the internal revenue laws, and who knows that such portion (if so used) would result in an understatement of the liability for tax of another person.

46. Jones prepared and aided or assisted in the preparation and filing of federal income tax returns and other documents that resulted in the understatement of her customers' tax liabilities.

47. As a result, Jones engaged in conduct subject to penalty under 26 U.S.C. § 6701.

48. Injunctive relief is appropriate to prevent recurrence of Jones's penalty conduct.

Count III: Injunction Under 26 U.S.C. § 7402

49. The United States incorporates by reference the allegations contained in paragraphs 1 through 48.

50. Courts may issue injunctions as may be necessary or appropriate for the enforcement of the internal revenue laws, even if the United States has other remedies available for enforcing those laws. 26 U.S.C. § 7402.

51. Jones substantially interfered with the enforcement of the internal revenue laws by promoting her "redemption" or "commercial redemption" tax-fraud scheme and filing frivolous federal tax returns and other documents on behalf of her customers.

52. As a result of Jones's misconduct, her customers fail to file proper tax returns and instead file frivolous refund claims.

53. Jones's conduct results in irreparable harm to the United States for which the United States has no adequate remedy at law.

54. Jones's conduct interferes with the proper administration of the Internal Revenue laws because it results in hundreds of frivolous filings that hinder the IRS's ability to determine the correct tax liabilities of her customers.

55. Unless enjoined by this Court, Jones will continue to promote and administer her tax-fraud scheme.
56. The United States is entitled to injunctive relief under I.R.C. § 7402(a) to prevent the recurrence of this misconduct.

WHEREFORE, Plaintiff, the United States of America, prays for the following relief:

- A. That the Court find that Jones has continually and repeatedly engaged in conduct subject to penalty under 26 U.S.C. §§ 6694, 6695, 6700, and 6701 and that injunctive relief is appropriate under 26 U.S.C. §§ 7402, 7407, and 7408 to bar Jones from acting as a tax return preparer and from engaging in conduct subject to penalty under 26 U.S.C. §§ 6694, 6695, 6700 and 6701;
- B. That the Court find that Jones has engaged in conduct that substantially interferes with the enforcement and administration of the internal revenue laws, and that injunctive relief against her is appropriate to prevent the recurrence of that misconduct pursuant to 26 U.S.C. §§ 7407 and 7402(a);
- C. That the Court, under 26 U.S.C. §§ 7402 and 7407, enter a permanent injunction permanently barring Jones from acting as a federal tax return preparer and from preparing or filing federal tax returns for others, and from representing others before the IRS;
- D. That the Court, under 26 U.S.C. §§ 7402 and 7407, enter a permanent injunction prohibiting Jones and her representatives, agents, servants, employees, attorneys, independent contractors, and anyone in active concert or participation with her, from directly or indirectly:

1. Preparing or filing, or assisting in, or directing the preparation or filing of any federal tax return or amended return or other related documents or forms for any other person or entity;
2. Giving tax advice or assistance to anyone for compensation;
3. Engaging in activity subject to penalty under 26 U.S.C. §§ 6694 or 6695;
4. Engaging in any other activity subject to penalty under the Internal Revenue Code; and
5. Engaging in other conduct that substantially interferes with the proper administration and enforcement of the internal revenue laws.

E. That this Court, under 26 U.S.C. §§ 7402 and 7408, enter a permanent injunction prohibiting Jones and her representatives, agents, servants, employees, and anyone in active concert or participation with her, from directly or indirectly by means of false, deceptive, or misleading commercial speech:

1. Organizing or selling tax shelters, plans or arrangements that advise or assist taxpayers to attempt to evade the assessment or collection of such taxpayers' correct federal tax;
2. Engaging in any other activity subject to penalty under 26 U.S.C. § 6700, including organizing or selling a plan or arrangement and making a statement regarding the excludability of income or any other tax benefit by participating in the plan that she knows or has reason to know is false or fraudulent as to any material matter;
3. Engaging in any activity subject to penalty under 26 U.S.C. § 6701; and

4. Directly or indirectly organizing, promoting, marketing, or selling any plan or arrangement that advises or encourages taxpayers to attempt to violate internal revenue laws or unlawfully evade the assessment or collection of their federal tax liabilities, including promoting, selling, or advocating the use of false Forms 1099 or other false IRS forms based on the false claims that:

- i. Taxpayers can draw on the Treasury of the United States to pay their tax debt or other debts using Forms 1099 or other documents;
- ii. Taxpayers can issue false Forms 1099 to a creditor and report the amount on the false Forms 1099 as income taxes withheld on their behalf, and;
- iii. Taxpayers have a secret account with the Treasury Department which they can use to pay their debts or which they can draw on for refunds through a process that is often called “redemption” or “commercial redemption.”

F. That this Court, under 26 U.S.C. § 7402, enter a permanent injunction prohibiting Jones from preparing her own federal income tax returns claiming false income tax withholding and refunds based on amounts shown in false Forms 1099;

G. That this Court, under 26 U.S.C. § 7402, enter a permanent injunction prohibiting Jones from filing, providing forms for, or otherwise aiding and abetting the filing of frivolous Forms 1040, Forms 1040X, or Forms 1099 for herself or others, including the notarization or signing of certificates of service or similar documents in connection with the frivolous tax returns;

- H. That this Court, under 26 U.S.C. § 7402, enter an injunction requiring Jones to contact by mail (and also by e-mail, if an address is known) all persons who have purchased any products, services or advice associated with the false or fraudulent tax scheme described in this complaint and inform those persons of the Court's findings concerning the falsity of Jones's prior representations and attach a copy of the permanent injunction against Jones;
- I. That this Court, under 26 U.S.C. § 7402, order Jones to provide to the United States a list of all persons who have purchased any products, services or advice from her in the past three years;
- J. That this Court allow the government full post-judgment discovery to monitor Jones's compliance with the injunction, and;
- K. That this Court grant the United States such other and further relief as the Court deems just and appropriate.

Dated: October 27, 2009.

Respectfully submitted,

THOMAS E. MOSS
United States Attorney

s/ James C. Strong
JAMES C. STRONG (ISB # 7428)
Trial Attorney, Tax Division
U.S. Department of Justice
Post Office Box 7238
Ben Franklin Station
Washington, D.C. 20044
Telephone: (202) 514-9953
Email: james.c.strong@usdoj.gov